

FINANCIAL MARKET CONDITIONS

September 30, 2006

Overview

The third quarter of 2006 saw a slowdown in the US economy, falling crude oil and gasoline prices, and a softening in real estate markets. After seventeen consecutive hikes in the Fed Funds overnight rate, the FOMC left it at 5.25% in its August 9 and September 20 meetings, citing the economic slowdown as a contributing factor in the decision. Stock and bond markets rallied strongly in anticipation of the Fed finally relaxing its stance on interest rates, which up to now was biased to tightening rates to dampen US economic expansion. July actually saw a pullback in US stocks in reaction to an increase in tension in the Middle East. However, the bull market returned in August and September as inflation fears eased, geopolitical tensions abated, natural disasters failed to materialize and commodity prices dropped. Crude oil prices traded at an intraday record \$78.40 (US dollar) per barrel in July, then slid to a quarter-end \$62.91 a barrel, a 14.9% drop. Natural gas prices also dropped; the September 29 close of \$5.62 USD per million BTU was 7.9% lower than its June 30 closing price. The fall in fuel prices canceled out increases in other consumer goods, resulting in a Consumer Price Index change of 0.0% for the third quarter. The benign interest rate environment helped US bond markets shake off bearish sentiment. Global markets in general benefited from optimism vis-a-vis the sustainability of the US economy's recovery; however, this optimism also fueled a resurgence in the US dollar against other currencies, dampening returns for US-based investors in overseas markets.

U.S. Economic Conditions

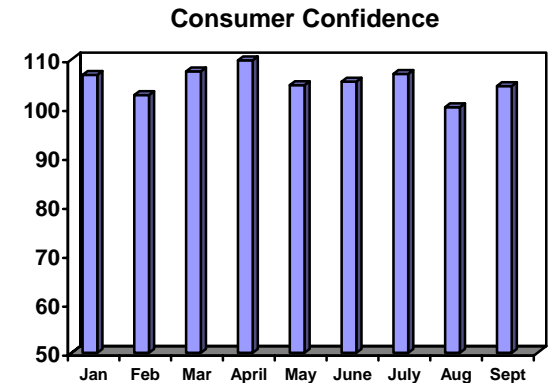
For the third quarter, gross domestic product, a measure of all goods and services produced in the US, grew at a modest annualized rate of 1.6%, according to the advance estimate from the Commerce Department. This pace was below the 2.2% consensus estimate and significantly lower than the 2.6% annualized growth rate of the previous quarter. The quarter's performance was also the weakest performance since the first quarter of 2003.

The slower growth pace was attributed to several factors, including a continued slowdown in homebuilding, weaker inventory spending, higher imports and lower state and local government spending. Partially mitigating these factors were higher investments in equipment, software durable goods, and increased federal government spending.

Homebuilding, or real investment in residential structures, posted a significant 17% annualized decline during the third quarter, accounting for a 1% decline in growth and causing residential investment to decline for the fourth straight quarter. This was also the sector's biggest decline since the beginning of 1991. The weakness in the housing market did not seem to put a damper on consumer spending, however, which increased 3.1% during the third quarter, ahead of the 2.6% growth of the second quarter.

The rate of inflation, as measured by the Consumer Price Index, declined 0.5% in September, due to a significant drop in energy prices, which declined 7.2% during the month. This drop followed 0.4% and 0.2% increases in July and August, respectively. Core inflation, which excludes volatile food and energy prices, increased 0.2% in September for the third consecutive 0.2% monthly increase in a row. Over the past twelve months, core inflation was 2.9% on an annualized basis.

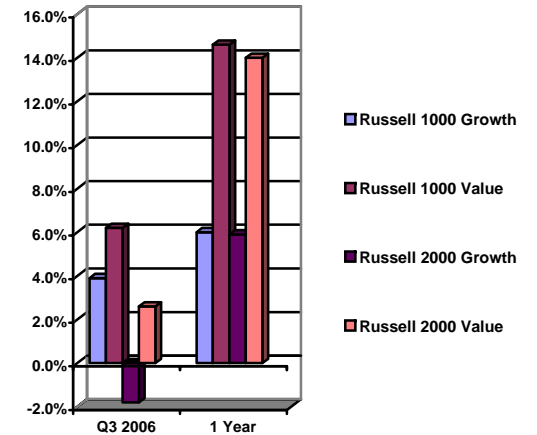
Job creation was much weaker than expected during the month of September, as the payroll employment increase of 51,000 was less than half of the consensus expectation. The biggest weakness in September was found in the manufacturing sector, followed by retail, temp help and government, however, the financial sector continued to expand. For the quarter, the three month average gain was 121,000 jobs, thanks in part to an upward August revision of 60,000 to 188,000. The unemployment rate declined slightly to 4.6% in September, down slightly from the 4.8% and 4.7% rates in July and August, respectively. Consumer confidence increased to 104.5 in September, ahead of the upwardly revised 100.2 level in August, but still below the 107.0 level in July.



Domestic Equities

The cooldown in the US economy drove many equity investors to favor stocks of large companies with the potential to sustain overseas revenues in the event of a more pronounced domestic economic pullback. As a result, in the third quarter of 2006 broad indexes with small-cap exposure such as the Russell 3000 Composite tended to underperform indexes with little small company exposure, such as the Standard & Poor's 500 Index (Russell 3000, 4.6%; S&P 500, 5.7%). The Russell 1000 Large Cap Index returned 5.1%, soundly exceeding the Russell 2000 Small Cap Index's 0.4%. As befits a market environment favoring defensive stocks, value-oriented equity strongly outperformed growth-oriented issues (Russell 1000 Value, 6.2%; Russell 1000 Growth, 3.9%; Russell 2000 Value, 2.6%; Russell 2000 Growth, negative 1.8%). Among sectors of the S&P 500 (Wilshire classifications), Finance at 8.1% and Technology at 8.1% were the best performers; Utilities stocks were also strong performers thanks to lower fuel costs (7.9%). Weak performance in Freight Service stocks contributed to the Transportation sector's poor return (negative 9.3%). Unsurprisingly, Energy stocks also gave back some of their recent strong returns in the third quarter (negative 1.6%).

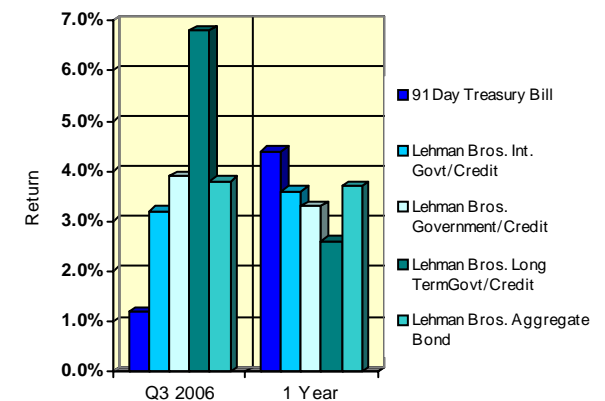
U.S. Equity Index Returns



Domestic Fixed Income

Inflation worries eased and bond yields fell at every point on the US Treasury yield curve in the third quarter. The yield on two-year Treasury issues fell 0.48% to 4.69%, while the yield on thirty-year Treasuries fell 0.42% to 4.8%. As befits a falling interest-rate market environment, long-term issues outperformed shorter-term paper (Lehman Long Government, 6.5%; Lehman 1-3 Year Government, 2.0%). Investors found corporate paper even more attractive as yields on government paper fell, leading to strong performance in the Credit sector (Lehman Credit, 4.5%; Lehman Government, 3.5%). Mortgage-backed securities also yielded strong performance (Lehman Mortgage, 3.6%). Although junk bond spreads over Treasuries inched higher over the quarter, lower interest rates eased default worries and pushed prices higher (Lehman High Yield, 4.1%).

U.S. Fixed Income Index Returns



Global Markets

The global stock and bond markets rallied from the troubles of the first half of 2006 with fairly strong performance in local market terms, although the rally in the US dollar lowered returns for US-based investors. As US interest rates at least paused in their recent climb, central banks in Europe and Asia refrained from raising their own lending rates, allowing local stock markets to recover. Europe benefited from optimism regarding regional investment opportunities as well as renewed vigor among corporate management in enhancing shareholder value (MSCI Europe 5.6%). Asian developed markets performance lagged that of Europe, with strong returns from Japan and Hong Kong countered by weaker returns in Australia and New Zealand (MSCI Pacific net, 0.4%). Emerging market stocks outperformed the broad developed market stocks over the quarter (MSCI Emerging Markets net, 4.9%; MSCI EAFE net, 3.9%); China and India were especially strong performers. Global debt markets followed the US' lead, rallying in a supportive interest rate and geopolitical environment (Lehman Global Aggregate, 2.2%; JP Morgan Emerging Markets Bond Plus, 6.9%).

**Selected Equity and Fixed Income Index Rates of Return
for Periods Ended September 30, 2006**

	Quarter	YTD	1 Year	3 Years	5 Years	10 Years
Equity Indices						
Standard & Poor's 500	5.7%	8.5%	10.8%	12.3%	7.0%	8.6%
Russell 3000	4.6	8.0	10.2	13.0	8.1	8.7
Russell 1000	5.1	8.0	10.2	12.8	7.6	8.8
Russell 1000 Growth	3.9	3.0	6.0	8.4	4.4	5.5
Russell 1000 Value	6.2	13.2	14.6	17.3	10.7	11.2
Russell 2000	0.4	8.7	9.9	15.5	13.8	9.1
Russell 2000 Growth	-1.8	4.2	5.9	11.8	10.2	4.0
Russell 2000 Value	2.6	13.3	14.0	19.0	17.0	13.4
MSCI EAFE (Net)	3.9	14.5	19.2	22.3	14.3	6.8
Fixed Income Indices						
Lehman Family:						
Aggregate	3.8	3.1	3.7	3.4	4.8	6.4
Government/Credit	3.9	2.7	3.3	3.1	5.0	6.5
Intermediate		3.0				
Government/Credit	3.2		3.6	2.6	4.3	6.0
Long Term Government/Credit	6.8	1.7	2.6	5.0	7.1	8.1
Government	3.5	2.6	3.3	2.8	4.3	6.2
Credit	4.5	2.9	3.4	3.5	5.8	6.8
Mortgage	3.6	3.6	4.2	3.9	4.5	6.3
Merrill Lynch High Yield Master II	4.1	7.3	8.0	9.0	10.2	6.6
Citigroup World Government Bond	1.4	4.2	2.2	4.1	7.3	5.3
Citigroup 3 Month T-Bill	1.2	3.5	4.4	2.6	2.2	3.7